STATE OF CALIFORNIA GRAY DAVIS, *Governor*

PUBLIC UTILITIES COMMISSION
505 VAN NESS AVENUE
SAN FRANCISCO, CA 94102-3298

April 3, 2003 **Agenda ID #2032**

TO: PARTIES OF RECORD IN APPLICATION 98-07-003

This is the proposed decision of Administrative Law Judge (ALJ) Barnett, previously designated as the principal hearing officer in this proceeding. It will not appear on the Commission's agenda for at least 30 days after the date it is mailed. This matter was categorized as ratesetting and is subject to Pub. Util. Code § 1701.3(c). Pursuant to Resolution ALJ-180, a Ratesetting Deliberative Meeting to consider this matter may be held upon the request of any Commissioner. If that occurs, the Commission will prepare and mail an agenda for the Ratesetting Deliberative Meeting 10 days before hand, and will advise the parties of this fact, and of the related ex parte communications prohibition period.

The Commission may act at the regular meeting, or it may postpone action until later. If action is postponed, the Commission will announce whether and when there will be a further prohibition on communications.

When the Commission acts on the proposed decision, it may adopt all or part of it as written, amend or modify it, or set it aside and prepare its own decision. Only when the Commission acts does the decision become binding on the parties.

Parties to the proceeding may file comments on the proposed decision as provided in Article 19 of the Commission's "Rules of Practice and Procedure." These rules are accessible on the Commission's website at http://www.cpuc.ca.gov. Pursuant to Rule 77.3 opening comments shall not exceed 15 pages. Finally, comments must be served separately on the ALJ and the assigned Commissioner, and for that purpose I suggest hand delivery, overnight mail, or other expeditious method of service.

/s/ Angela K. Minkin
Angela K. Minkin, Chief
Administrative Law Judge

ANG:avs

Decision **PROPOSED DECISION OF ALJ BARNETT (Mailed 4/3/2003)**

**BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA**

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| Application of Pacific Gas and Electric Company for Verification, Consolidation, and Approval of Costs and Revenues in the Transition Revenue Account. | Application 98-07-003 (Post PX Direct Access Credits) (Filed July 1, 1998) |

(See Appendix A for appearances)

# OPINION ADOPTING A POST POWER EXCHANGE DIRECT ACCESS CREDIT FOR PACIFIC GAS AND ELECTRIC COMPANY AND SOUTHERN CALIFORNIA EDISON COMPANY

## I. Summary

This is another decision that addresses the direct access (DA) credit. We recently set forth the background leading up to this installment in Decision (D.) 02-07-032, which we repeat for clarity.[1] This proceeding is to determine a new method of computing the charges to be paid by direct access customers to Pacific Gas and Electric Company (PG&E) and SCE, and to determine the reasonableness of the utilities' current DA credit methods. This decision finds reasonable the direct access credit methods used by PG&E and SCE since the

[1] D.02-07-032 dealt with Southern California Edison (SCE). This proceeding deals with both SCE and PG&E, but the background facts are the same for both utilities. We have modified the material accordingly.

demise of the Power Exchange (PX) and approves of "bottoms-up" billing for direct access customers. In bottoms-up billing, the utilities bill only for distribution and transmission service; the customer purchases electricity from a third party. Thus, under the "bottoms-up" approach, customers pay for the services they purchase from the utilities, including any nonbypassable charges. This is in contrast to DA customers paying the same charges as bundled customers and then receiving a credit.

## II. Background

Since 1998, PG&E and SCE have offered service to two distinct classes of customers. Bundled service customers received the full range of electric services from the utilities, which include energy procurement and delivery. PG&E and SCE customers could also choose, under the DA option, to purchase energy from an electric service provider (ESP). PG&E and SCE continue to deliver electricity to both DA and bundled service customers.

### A. Rate Freeze

Total rates were frozen at levels in effect on June 10, 1996 for all customers. Bundled service customers paid these frozen rates for the duration of the transition period (January 1, 1998 through March 31, 2002 or a Commission-authorized earlier end date). These frozen tariff rates included a generation rate component. The generation rate was unbundled into a market price and a competition transition charge (CTC) component. The CTC was calculated residually as the difference between the fixed generation rate component and the market price, where the market price was based on the utility's cost of procuring power from the PX and the California Independent System Operator (ISO). All customers pay the CTC and the CTC revenues were

to be used to pay for the utility's stranded generation costs, also known as transition costs.

### B. The Avoided Cost Credit

The utilities calculated a market price for billing purposes utilizing the cost and quantities of power purchased from the PX. This PX price was used to determine the contribution to the recovery of CTC (when compared to the generation rate component of frozen rates) and also represented the utilities' avoided cost of procuring energy. The PX component of the generation rate was either applied to recover the cost of purchasing power for bundled service customers or given as a credit to DA customers. The credit reflected the fact that DA customers had chosen to procure their energy through an ESP rather than the utility. So long as the market price, or DA credit, remained below the generation component of the customer's frozen rate, the DA customer continued to make a contribution to CTC in exactly the same manner as a similarly situated bundled service customer.

### C. The Zero Minimum Bill Provision

Because the DA credit was based on the market price from the PX, it was possible that the credit would exceed either the generation rate component or the entire bill. If the PX credit exceeded the generation rate component, there was a negative CTC, *i.e.*, no contribution to recovery of stranded costs. If the PX credit exceeded the entire amount of the bill, meaning that the PX credit was greater than the sum of the generation, distribution, transmission, public purpose, and the other rate components, there would be a negative bill. In other words, the DA customer would receive a credit for the entire utility bill. This is also known as a "credit" bill.

Prior to June 1999, under the adopted tariffs, DA customers receiving the PX credit could experience, at a minimum, a monthly bill of $0. In D.99-06-058, the Commission eliminated the zero minimum bill provision. The elimination of the zero-minimum bill provision allowed DA customers to receive the entire PX credit even if it resulted in a negative (credit) bill. Prior to market dysfunctions in mid 2000, PX credits in excess of total monthly charges were generally carried over to succeeding months and were netted against positive bills.

The dysfunction of California energy markets in 2000 through early 2001, undermined the original basis for calculating the DA credit. The prices charged the utilities during the waning days of the PX were substantially higher than the cost of producing the energy; were regularly higher than the generation component of frozen rates; and in fact, were frequently so high that the DA credit exceeded the entire amount of a DA customer's bill for the services the DA customer did take from the utility and the generation rate component. The PX collapsed in January 2001. Afterwards, consistent with Commission decisions adopting an interim accounting methodology for utility retained generation (URG) and payment mechanisms for recovery of the costs of Department of Water Resources (DWR) power purchases, the utilities based their DA credit on a combination of the costs of URG and DWR-provided power as an approximation of the cost of energy. These changes in the California electricity market require a new method of computing direct access charges.

## III. PG&E's Proposal

PG&E proposes to calculate a credit to direct access customers as follows: For the period December 28, 2000 to January 18, 2001, PG&E would use the Schedule PX price to set the DA credit, with the energy cost capped at the

level ultimately determined by the Federal Energy Regulatory Commission (FERC) to be just and reasonable. PG&E believes issuing bill adjustments to the DA customers and ESPs who received the benefit of a DA credit that was based on unjust and unreasonable prices is justified for this period to adhere to the avoided cost principle and prevent the shifting of costs from DA customers to other ratepayers. For periods subsequent to January 18, 2001, the date PG&E could no longer purchase energy from the PX, PG&E seeks authority to adopt the DA credits for past periods as determined by PG&E using the combination of URG and DWR costs for the period after January 18, 2001, continuing through PG&E's implementation of bottoms-up billing for DA customers. Bottoms-up billing charges DA customers only the distribution and transmission component of the bundled customer bill.

### A. The Period December 28, 2000 to January 18, 2001

PG&E proposes that for the period December 28, 2000 to January 18, 2001, DA customers retain the benefit of DA credits already calculated, but that such credits should be limited by FERC's final determination of what the just and reasonable rates for wholesale energy during that period were. FERC is considering those rates in a proceeding affecting bulk power markets and wholesale energy prices in California.[2]

PG&E argues that its proposal does not violate any rule against retroactive ratemaking. It is based on simple fairness and sound policy. The DA credit during the period December 28, 2000 – January 18, 2001 was determined based on the cost of energy that PG&E purchased from the PX and ISO. When it

[2] *San Diego Gas and Electric Company v. Sellers of Energy*, 92 F.E.R.C. (CCH)¶61,172 (Aug. 23, 2000), reh'g pending.

approved PG&E's Schedule PX tariff, the Commission approved a credit calculation for DA customers that was based directly on FERC rates (as passed through to PG&E by the PX and the ISO). PG&E says that if FERC changes those rates retroactively, through refund and as the FERC announced on November 1, 2000 that it may do[3] --- the same considerations of policy and fairness which led the Commission to base the credit on actual energy costs compel a retroactive adjustment to DA credits.

PG&E asserts that if FERC determines that market prices paid to generators and used in the DA credit calculation were unjust and unreasonable, it would require the ISO to recalculate hourly prices, and the ISO and PX to rerun the settlement/billing process. What remains for this Commission to do is merely to recognize that a billing adjustment is required to give effect to the result of the FERC's investigation. In the opinion of PG&E, such an adjustment would not be retroactive ratemaking. First, this proceeding is not a general rate proceeding; thus, the prohibition against retroactive ratemaking does not apply. *See* Southern Cal. Edsion Co. v. Pub. Utils. Com., (1978) 20 Cal 3d 813, 816. Second, what PG&E proposes is not a change in a rate, but a true-up of its calculation under an existing effective tariff. PG&E believes that if it were the case that PG&E's energy costs during December 2000 and January 2001 were found to be higher than what was used to calculate DA credits, DA customers would be requesting an upward adjustment in their credits.

New West Energy Corporation (New West) and the Alliance for Retail Energy Markets and the Western Power Trading Forum (AReM/WPTF) oppose

[3] *See San Diego Gas and Electric Co. v. Sellers of Energy* 93 F.E.R.C. (CCH) ¶61, 121 at p. 61,370 (Nov. 1, 2000).

PG&E's proposal on the grounds that (1) it constitutes retroactive ratemaking and (2) retroactive rebilling would seriously impact DA customers. They argue that retroactive rebilling would be a nightmare for DA customers. The impact of allowing retroactive rebilling has far reaching impacts on DA customers who include the price of energy in their services and products. Those DA customers could not recoup increased costs two years later. The process to find past DA customers and recompute bills would be confusing, difficult, and inequitable. Some DA customers would see increased costs, while others who had moved out of state or could not be located for whatever reason, would avoid the effect of the recalculation. AReM/WPTF believe that the interests of ratepayers are best served by minimizing the need to revisit the past and imposing costs on customers long after they are able to make economic decisions based on a realistic understanding of their costs.

We agree with AReM/WPTF. In our opinion it would be unreasonable to recompute the DA credit should FERC order refunds. We are confronted, initially, with three unknown factors: whether FERC will order refunds: when FERC will order refunds ( and when the order become final), and the amount of those refunds.[4] As of this writing, FERC has the matter under consideration. Any order of refunds, if substantial, is expected to be appealed. It is impossible to predict the date of a final order. The period in question, December 28, 2000 to January 18, 2001, is two years old and counting. It is unfair for ratepayers who paid their utility bills two years ago to be subject to an unknown liability to be

[4] When we speak of refunds in this context we refer not to money going back to DA customers, but to a recomputation of their credit. If a refund is ordered the credit

*Footnote continued on next page*

paid at an unknown future date. We need not elaborate on the intensive effort required by PG&E to recompute individual bills nor the intensive efforts and spent resources of end users to verify those recomputed bills. Because we deny PG&E's proposal we do not reach the question of whether approval of the proposal would constitute retroactive ratemaking.

### B. The Period January 19, 2001 to the Implementation of Bottoms-Up Billing

PG&E proposes to use its current methodology for calculating the DA credit for the period from and including January 19, 2001 to the implementation date of a final Commission order in this proceeding. PG&E maintains that its current methodology strikes a balance between the philosophical underpinnings of the DA credit, which was based on avoided cost assuming a functional, efficient market for energy, and Commission efforts to deal with the dysfunctionality of that market after the demise of the PX.

PG&E states that its ability to purchase electricity in excess of its own generation including must-take generation from the PX's day-ahead and day-of markets ended effective January 18 and January 19, 2001, respectively. On January 31, 2001, the Commission issued D.01-01-061, adopting an interim accounting methodology for URG, which was subject to later adjustment and true-up. Because of the immediate need for a reasonable cost proxy for utility retained generation, PG&E calculated the Schedule PX price using an estimate of its cost-of-service for its retained generation. In D.01-03-081, the Commission elaborated on the payment mechanisms used for recovery of the costs of DWR

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would have been less and the DA customer would have been overpaid by PG&E thereby causing a repayment to PG&E.

power sales to PG&E's end-user customers. PG&E has used those payment amounts, as modified by subsequent decisions, as the basis for the pricing of DWR-provided power under Schedule PX.

Thus, since the demise of the PX, PG&E has used a measure of the cost of energy to determine the DA credit, but (due to the same demise) is not based on its actual avoided costs. In place of the forward-market price of power from the PX and other avoided costs, PG&E now uses a weighted average generation cost for retained generation, power purchases and DWR power, increased by ISO administrative costs. PG&E also adjusts prices for distribution losses, the uncollectible allowance, and a procurement adder as required by Schedule PX. PG&E does not propose to retroactively adjust credits that were rendered using its current methodology. No party objects to PG&E's proposal. It is a reasonable approach that recognizes the market realities and will be adopted.

### C. Bottoms-Up Billing

PG&E proposes to provide bottoms-up billing to DA customers, once its new billing system is in place. Under this method, there is no credit. DA customers would pay the sum of transmission (including reliability services), distribution, nuclear decommissioning, public purpose programs, and the fixed transition amount (FTA), where applicable, as well as any nonbypassable charges approved by the Commission for DA customers. DA customers would not pay the average three-cent per kWh and one-cent per kWh generation surcharges; however, they would pay charges the Commission may impose on them, for example, DWR bond charges, applicable DWR power costs, PG&E's ongoing CTC, and PG&E's historic uncollected charges.

In order to implement bottoms-up billing for DA customers, PG&E proposes to amend its tariff to include in distribution rates the costs of the

nonfirm discounts, rate limiter adjustments, and power factor adjustments (including standby reactive charges). Since these costs had previously been allocated to generation, they could be avoided by a DA customer billed on a bottoms-up basis. By putting these costs in distribution rates, DA customers will not avoid paying for these discounts. This was approved in the Phase 2 Post-Transition Electric Ratemaking (PTER) decision (D.00-06-034, Ordering Paragraph No. 14). No party objects to PG&E's proposal. This approach is reasonable because it complies with previous decisions and it will be adopted.

## IV. SCE's Proposals

### A. The Period January 19, 2001 to June 2, 2001

On January 19, 2001, SCE ended its participation in the PX markets. As a result, SCE could no longer utilize the PX price to calculate the DA credit. Thus, SCE was compelled to modify its DA credit methodology to reflect the fact that it was no longer procuring power from the PX, but rather from a number of sources. SCE, therefore, modified its DA credit methodology to rely instead on a weighted average energy price. SCE used this modified methodology until June 3, 2001. SCE requests that the Commission ratify its DA credit calculation between January 19, 2001 and June 2, 2001. No party objects. We agree that it is reasonable because it uses an appropriate calculation the DA credit.

### B. The Period June 3, 2001 to Implementation of Bottoms-Up Billing

Since June 3, 2001, SCE has utilized a DA credit calculation based on the generation rate of the customer's otherwise applicable tariff (OAT). Under Schedule PE-Procured Energy, the DA credit is set at the generation component of the OAT, adjusted for charges or credits. SCE requests that the Commission ratify its modified OAT generation methodology employed since June 3, 2001.

No party objects. Again, we agree that this is a reasonable approach and we approve it.

SCE proposes that for the remainder of the Rate Repayment Period (as defined in the Settlement)[5] Historical Procurement Charges (HPC), and all other authorized non-bypassable charges, should be subtracted from the generation component of the DA customers OAT before it is credited to them. SCE says the Commission has already signaled its approval of this mechanism in the findings of fact D.02-07-032:

> "SCE will modify the currently effective DA credit calculation by subtracting the HPC as adopted from the generation rate of the DA customers' OAT before it is credited to them. The HPC will have the effect of reducing future credits."[6]

SCE, therefore, urges the Commission to find that until bottoms-up billing is adopted at the end of SCE's Rate Repayment Period, SCE's HPC, and all other authorized non-bypassable charges, should be subtracted from the generation component of the DA customers' OAT before it is credited to them. No party objects. This methodology appropriately ensures that DA customers pay the required nonbypassable charges. It is reasonable and will be adopted.

### C. Bottoms-Up Billing

SCE asserts that nearly every party to this proceeding agrees that the best prospective approach is to avoid the crediting methodology entirely by moving to a bottoms-up billing approach. Under this approach, DA customers'

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[5] The Rate Repayment Period is defined as September 1, 2001 to the earlier of December 31, 2003 or when SCE recovers its Procurement Related Obligation Account (PROACT) balance. For a detailed description of the Settlement, the HPC, and PROACT, *see* D.02-07-032.

[6] *See* D.02-07-032, Finding of Fact 10.

bills would be based on the services they purchase from the utility, plus any nonbypassable charges, instead of paying the same total charges as bundled service customers and then receiving a credit. SCE submits that there is broad support for this approach and that the Commission should authorize a bottoms-up approach for SCE at the end of its Settlement Rate Repayment period. SCE's proposal is the same as PG&E's. It is reasonable and will be adopted.

## V. The 10% Discount for Residential and Small Commercial Customers

Section 368 of the Public Utilities Code, among other things, froze rates at their June 10, 1996 levels through no later than March 31, 2002, and provided an immediate 10% reduction of those rate levels for residential and small commercial customers. In 2001, Section 368.5[7] of the Public Utilities Code was added, which states, in part, that, "[T]he commission may not subject those residential and small commercial customers to any rate increases or future rate obligations solely as a result of the termination of the 10% rate reduction." These references to rate levels implicitly refer to total bundled rate levels, since total rates paid by DA customers are unknown, fluctuate over time, and differ from customer to customer.

PG&E proposes a slightly different treatment of the 10% reduction than SCE proposes. PG&E currently provides the 10% reduction to DA residential

[7] Section 368.5(a) states that the Commission may not subject residential and small commercial customers to any rate increase or future rate obligations solely as a result of the termination of the 10% rate reduction. Section 368.5(b) retains the Commission's authority to increase rates to those customers for reasons other than the termination of the 10% rate reduction. Therefore, bundled service or DA customers cannot receive a rate increase solely by depriving either group of the 10% rate reduction.

and small commercial customers. PG&E argues that this 10% reduction is eliminated when bottoms-up billing is established because rates will not have been increased "solely as a result of the termination of the 10% rate reduction." SCE's current DA billing methodology, which it proposes to apply until Settlement Rates are no longer in effect, provides a 10% reduction to residential and small commercial DA customers. The Commission has directed SCE to maintain the 10% rate reduction for at least the duration of the Settlement Rates. Once the Settlement Rates disappear, however, and SCE moves to a bottoms-up calculation, the 10% rate discount for residential and small commercial DA customers may be eliminated.

To sum up: today both PG&E and SCE provide the 10% reduction to their DA residential and small commercial customers. This will continue for PG&E until it implements bottoms-up billing at which time it may be eliminated. For SCE the 10% reduction will continue for the duration of the Settlement Rates (which are expected to end by mid-2003). At that time SCE will implement bottoms-up billing and may eliminate the 10% reduction.

We agree with PG&E and SCE that upon implementation of bottoms-up billing a rate increase for DA customers will not result "solely as a result of the termination of the 10% rate reduction on March 31, 2002." It will result from going to bottoms-up billing.

## VI. The Audit of the DA Credit Process

In its rebuttal testimony AReM/WPTF requests an ongoing audit process for the DA credit. AReM/WPTF claims that this audit is necessitated by the wide disparity in methods proposed by the two utilities and the variation in credits. SCE and PG&E strongly disagree and submit that an ongoing audit of their DA credit process would be a blatant waste of time and resources.

Since June 3, 2001, SCE has provided a DA credit equal to the generation component of the customer's OAT. SCE proposes to continue this practice until a move to bottoms-up rates, after which, there will be no DA credit. SCE contends that the generation component of the OAT is transparent and easily verifiable. In other words, there is nothing to audit under SCE's preferred approach. There are no assumptions built into SCE's approach. The credit is equal to the published generation component of the OAT.

PG&E argues that an audit would be not only pointless, but also expensive. A previous DA credit audit authorized by D.99-06-058 cost more than $1.5 million and discovered only a few minor variances in the monthly reports. PG&E maintains that the cost of that audit far exceeded any benefits. PG&E asserts it is not reasonable for all utility ratepayers to have to pay to provide comfort to a small subset of DA customers in the form of an unnecessary audit.

We agree with PG&E and SCE. There is not a scintilla of evidence in this proceeding to show that an audit is necessary. There is no Commission staff report which raises any questions regarding the accuracy of utility DA credit accounting. Nor have any DA customers revealed a problem with utility DA credit accounting. Further, we have no intention of ordering an audit for the benefit of a small class of customers to be paid for by all utility customers. Should a DA customer find a discrepancy in its utility bill, the Commission's complaint procedure will afford redress.

## VII. Comments of Proposed Decision

The proposed decision of the Administrative Law Judge was mailed to the parties in accordance with Pub. Util. Code § 311(d) and Rule 77.1 of the Rules of Practice and Procedure. Comments were received on _____.

## VIII. Assignment of Proceeding

Carl Wood is the Assigned Commissioner and Robert Barnett is the assigned Administrative Law Judge in this proceeding.

## Findings of Fact

1. Customers who purchase bundled service from their serving utility pay an electricity charge to cover the utility's power supply costs. For those bundled service customers, the total bundled bill includes charges for all utility services, including distribution and transmission as well as electricity.

2. A direct access customer receives distribution and transmission service from its serving utility, but purchases electricity from its ESP.

3. The Power Exchange credit is the billing credit that DA customers receive which reflects its serving utility's costs of procuring power. DA customers receive this credit because they purchase their power from an ESP.

4. In January 2001, the PX collapsed, ending the utilities' ability to purchase electricity in excess of their own generation from the PX's markets effective January 19, 2001.

5. On January 31, 2001, the Commission issued D.01-01-061 adopting an interim accounting methodology for utility retained generation (URG), which was subject to later adjustment and true-up.

6. In D.01-03-81, the Commission elaborated on the payment mechanisms used for recovery of the costs of DWR power sales to end user customers.

7. After it could no longer purchase energy from the PX, PG&E used a cost of energy to calculate the PX credit that was based on an estimate of cost-of-service for its URG, and its payments for DWR-provided power.

8. Bottoms-up billing for DA customers means that DA customers' bills are based on the services they purchase from their serving utility, plus any nonbypassable charges.

9. PG&E proposes to eliminate the DA credit and bill DA customers on a bottoms-up basis.

10. PG&E's billing system will need to be modified to accommodate bottoms-up billing.

11. Until bottoms-up rates are adopted at the end of SCE's Rate Repayment Period, SCE's HPC, and all other authorized non-bypassable charges, should be subtracted from the generation component of the DA customers' OAT before it is credited to them.

12. An audit of the DA credit is not needed.

## Conclusions of Law

1. The method used by PG&E to determine the DA credit after the end of the PX to the date on which it implements bottoms-up billing is just and reasonable.

2. It is unreasonable to require DA customers to have their DA credit recomputed should FERC order refunds as it will subject DA customers to an unknown liability to be paid at an unknown future date.

3. The DA credit methodologies that SCE implemented from January 19, 2001 through the present are reasonable on the basis that they ensured that DA customers received a credit exactly equal to the rate that SCE charged bundled service customers for energy procured on their behalf.

4. It is reasonable to replace the DA credit with bottoms-up billing.

5. Upon implementation of bottoms-up billing, a rate increase for DA customers will not result solely as a result of the termination of 10% rate reduction; instead, this is a result of moving to bottoms-up billing.

6. This decision should be effective today to provide certainty to DA customers and to the utilities.

## O R D E R

**IT IS ORDERED** that:

1. Pacific Gas and Electric (PG&E) shall implement bottoms-up billing within 60 days from the effective date of this decision.

2. Southern California Edison (SCE) shall implement bottoms-up billing at the end of its Rate Repayment Period.

3. Within 30 days of the effective date of this order, PG&E and SCE shall file an Advice Letter with revised tariff sheets to implement the authority granted in this decision. The revised tariff sheets shall become effective on filing, subject to a finding of compliance by the Energy Division, and shall comply with General Order 96-A. The revised tariff sheets shall apply to service rendered on or after their effective date.

This order is effective today.

Dated _____, at San Francisco, California.